

## C H A P T E R - I

### I N T R O D U C T I O N

Over the last century or so in all the countries, irrespective of their level of economic development, there has been a significant increase in the magnitude and variety of governmental activities even within the framework of a private enterprise capitalism. The increasing importance of the principle of welfare state and the consequent decline of the doctrine of laissez-faire, the increasing disbelief in the efficacy of the "invisible hand" in ensuring an optimum allocation of economic resources, the emergence of influential groups in the shape of monopolies, oligopolies and business combinations and, last but not the least, the immense necessity of maintaining full employment and a steady rate of growth under capitalism have all contributed significantly in the increasing role of the state in a private enterprise economy.

The Government of India usually regulates the private enterprise economy by two means, namely controls and incentives. Licensing, quota fixation in production, restrictions on prices, regulation on foreign trade, both import and export, involvement in decision making process in the enterprises and regulation in the flow of capital are some of the examples through which the Government generally attempts to control the private enterprises.

Incentives, on the other hand, are meant for channelising the resources of the private enterprise economy on their self-initiative, into the desired direction, befitting the framework of national plans. Such incentives in India, are generally seen, specially after independence, in the form of different fiscal measures, both financial and non-financial, like, tax concessions, cheaper rates of borrowing, concessional treatment in importing raw materials, guaranteed power supply and allowance of proper priority in the development of infrastructure.

The importance of tax revenue as a major source of fund has been well recognised in all the countries in the world. It can be noted from a study for the period 1965-76 made by IMF among member countries of the Organisation for Economic Co-operation and Development (OECD) that the countries relied mainly on three groups of taxes - taxes on income and profits, social security contributions and taxes on goods and services for their economic development.<sup>1</sup> So what can be seen is, that at present, the positive role of any government, at least for initiating the minimum economic programmes in a country, cannot be denied. As an inevitable needs for initiating such economic efforts like

---

1. I.M.F. Survey - 'Ratio of Tax Revenues to G.D.P. shows Rise in Many OECD Countries in Period 1965-76', Jan. 23, 1978.

other countries, in India also, there has been a substantial increase in the aggregate receipts and disbursements on revenue and capital accounts in recent years. In India tax revenue represents more than 80 per cent contribution of total revenue receipts.

### 1.1. Importance & Growth of Taxes:

The importance of tax as a source of revenue has been increasing gradually, specially after the Second Five Years Plan in India. The quantum of tax, both direct and indirect taken together, had risen from Rs. 627 crores to Rs. 15,528 crores since pre-plan year in 1950-51 to the end of Fifth Plan period in 1978-79 (Table 1.1). This represents more than twenty-four times increase in revenue earnings over the period of twenty-eight years. The corresponding earning figures were Rs. 17,683 crores in 1979-80 and the revised estimates and the budgeted estimates for the years 1980-81 and 1981-82 came to be Rs. 19,694 and Rs. 22,191 crores respectively. Though the shares representing central taxes and state taxes of total tax revenues almost remaining same, as 64.6 per cent and 35.4 per cent in 1950-51 and 66.1 per cent and 33.9 per cent in 1981-82, the importance of direct taxes over indirect taxes as a source of revenue to the Government is seen to be diminishing over the years and the

Table I.1

Growth of Taxes in India : 1950-51 to 1981-82  
(Centre, States and Union Territories)

(Rs....Crores)

| Period                              | Year    | Direct Taxes |           | Indirect Taxes |           | Total Taxes |            | Central Taxes |           | State Taxes |           |
|-------------------------------------|---------|--------------|-----------|----------------|-----------|-------------|------------|---------------|-----------|-------------|-----------|
|                                     |         | 1            | 1a=% of 3 | 2              | 2a=% of 3 | 3=(1+2)     | 3a=(1a+2a) | 4             | 4a=% of 3 | 5           | 5a=% of 3 |
| Pre-Plan Year                       | 1950-51 | 231          | (36.8)    | 396            | (63.2)    | 627         | (100)      | 405           | (64.6)    | 222         | (35.4)    |
| First Plan -<br>Terminal Year       | 1955-56 | 259          | (33.7)    | 509            | (66.3)    | 768         | (100)      | 458           | (63.2)    | 283         | (36.8)    |
| Second Plan -<br>Terminal Year      | 1960-61 | 402          | (29.8)    | 948            | (70.2)    | 1,350       | (100)      | 895           | (66.3)    | 455         | (33.7)    |
| Third Plan                          | 1961-62 | 449          | (29.1)    | 1,094          | (70.9)    | 1,543       | (100)      | 1,054         | (68.3)    | 489         | (31.7)    |
|                                     | 1962-63 | 560          | (30.0)    | 1,304          | (70.0)    | 1,865       | (100)      | 1,285         | (68.9)    | 580         | (31.1)    |
|                                     | 1963-64 | 693          | (29.8)    | 1,632          | (70.2)    | 2,325       | (100)      | 1,633         | (70.2)    | 692         | (29.8)    |
|                                     | 1964-65 | 742          | (28.5)    | 1,857          | (71.5)    | 2,599       | (100)      | 1,821         | (70.1)    | 778         | (29.5)    |
| Third Plan -<br>Terminal Year       | 1965-66 | 734          | (25.1)    | 2,188          | (74.9)    | 2,922       | (100)      | 2,061         | (70.5)    | 861         | (29.5)    |
| Annual Plans                        | 1966-67 | 767          | (23.5)    | 2,494          | (76.5)    | 3,261       | (100)      | 2,307         | (70.7)    | 954         | (29.3)    |
|                                     | 1967-68 | 780          | (22.6)    | 2,676          | (77.4)    | 3,456       | (100)      | 2,353         | (68.1)    | 1,103       | (31.9)    |
| Base year for<br>the Fourth<br>Plan | 1968-69 | 840          | (22.3)    | 2,919          | (77.7)    | 3,759       | (100)      | 2,510         | (66.8)    | 1,249       | (33.2)    |
| Fourth Plan                         | 1969-70 | 963          | (22.9)    | 3,237          | (77.1)    | 4,200       | (100)      | 2,823         | (67.2)    | 1,377       | (32.8)    |
|                                     | 1970-71 | 1,009        | (21.2)    | 3,743          | (78.8)    | 4,752       | (100)      | 3,207         | (67.5)    | 1,545       | (32.5)    |
|                                     | 1971-72 | 1,171        | (21.0)    | 4,404          | (79.0)    | 5,575       | (100)      | 3,872         | (69.5)    | 1,703       | (30.5)    |
|                                     | 1972-73 | 1,346        | (20.9)    | 5,090          | (79.1)    | 6,436       | (100)      | 4,505         | (70.0)    | 1,931       | (30.0)    |

Contd.....

Table - I.1 (Contd.....) Growth of Taxes

|                                 |         |       |        |        |        |        |       |        |        |       |        |
|---------------------------------|---------|-------|--------|--------|--------|--------|-------|--------|--------|-------|--------|
| Fourth Plan -<br>Terminal Year  | 1973-74 | 1,552 | (21.0) | 5,836  | (79.0) | 7,389  | (100) | 5,070  | (68.6) | 2,319 | (31.4) |
| Fifth Plan                      | 1974-75 | 1,834 | (19.9) | 7,389  | (80.1) | 9,223  | (100) | 6,322  | (68.5) | 2,901 | (31.5) |
|                                 | 1975-76 | 2,493 | (22.3) | 8,689  | (77.7) | 11,182 | (100) | 7,609  | (68.5) | 3,573 | (32.0) |
|                                 | 1976-77 | 2,585 | (21.0) | 9,747  | (79.0) | 12,332 | (100) | 8,271  | (67.1) | 4,061 | (32.9) |
|                                 | 1977-78 | 2,680 | (20.2) | 10,557 | (79.8) | 12,332 | (100) | 8,271  | (67.1) | 4,379 | (33.1) |
| Fifth Plan -<br>Terminal Year   | 1978-79 | 2,851 | (18.4) | 12,677 | (81.6) | 15,528 | (100) | 10,525 | (67.8) | 5,003 | (32.2) |
| Base year for<br>the Sixth Plan | 1979-80 | 3,096 | (17.5) | 14,587 | (82.5) | 17,683 | (100) | 11,974 | (67.7) | 5,709 | (34.3) |
| Sixth Plan (R.E.)               | 1980-81 | 3,459 | (17.6) | 16,235 | (82.4) | 19,694 | (100) | 13,133 | (66.7) | 6,561 | (33.3) |
| (B.E.)                          | 1981-82 | 3,788 | (17.1) | 18,403 | (82.9) | 22,191 | (100) | 14,663 | (66.1) | 7,523 | (33.9) |

Source : Eastern Economist. Budget Number, 1982,  
V. 78 No. 11, March 19, 1982.

B.E. Budget Estimate  
R.E. Revised Estimate.

share of direct tax in percentage dropped from 36.8 in 1950-51 to 17.1 in 1981-82. The share of indirect tax on total tax revenues correspondingly increased from 63.2 per cent in 1950-51 to 82.9 per cent in 1981-82. It would be our endeavour to highlight the importance of corporate tax as a source of revenue out of total direct taxes and to see whether corporate tax itself became the major contributory source in the comparative diminishing growth of revenues from direct taxes.

#### 1.2. Importance of direct tax and corporation tax in total central taxes:

A Table bearing No. I.2 has been prepared and analysed for our purpose. The period covered in our analysis is from 1970-71 to 1982-83. Out of the total amount of central taxes of Rs. 13180 crores in 1980-81, the direct taxes and indirect taxes responded to 22.7 per cent and 77.3 per cent respectively. The corresponding shares in 1970-71 were 27.1 per cent and 72.9 per cent. That might show the diminishing trend of revenue earnings through direct taxes in comparison with the indirect one. Of course the revised estimates and the budgeted estimates for 1981-82 and 1982-83 financial years highlighted the greater proportion of direct tax collections over the past few years. Out of total direct taxes the share of corporation tax is gradually increasing in amount and in proportion; 42.6 per cent of total central direct taxes was raised through

Table - I.2

Growth of Central Taxes : 1970-71 to 1982-83

(Gross Collection)

(Rs. ... Crores)

| Year    | Corporation Tax<br>(2) (2a)=<br>% of (5) % of (3) | Total Direct<br>Taxes<br>(3) (3a)=<br>% of (5) | Total Indirect<br>Taxes<br>(4) (4a)=<br>% of (5) | Total Central<br>Taxes<br>(5)=(3) + (4) | N.I.<br>(Net)<br>(6) | % of N.I.<br>(Current Prices)<br>(7)=(5) as % of<br>(6) |
|---------|---|--|--|---|----------------------|---|
| 1970-71 | 371 (11.6)  | 870 (27.1)                                     | 2,337 (72.9)                                     | 3,207                                   | 34,235               | 9.37  |
| 1971-72 | 472 (12.2)  | 1,047 (27.0)                                   | 2,325 (73.0)                                     | 3,372                                   | 36,573               | 10.59   |
| 1972-73 | 553 (12.4)  | 1,238 (27.5)                                   | 3,272 (72.5)                                     | 4,510                                   | 40,270               | 11.20   |
| 1973-74 | 583 (11.5)  | 1,379 (27.2)                                   | 3,694 (72.8)                                     | 5,073                                   | 50,424               | 10.06   |
| 1974-75 | 710 (11.2)  | 1,650 (26.1)                                   | 4,672 (73.9)                                     | 6,322                                   | 59,446               | 10.63   |
| 1975-76 | 862 (11.3)  | 2,205 (29.0)                                   | 5,404 (71.0)                                     | 7,609                                   | 62,069               | 12.23   |
| 1976-77 | 984 (11.9)  | 2,328 (28.1)                                   | 5,943 (71.9)                                     | 8,271                                   | 67,083               | 12.33   |
| 1977-78 | 1,221 (13.8)                                      | 2,406 (27.2)                                   | 6,452 (72.8)                                     | 8,858                                   | 75,935               | 11.67   |
| 1978-79 | 1,252 (11.9)                                      | 2,528 (24.0)                                   | 7,997 (76.0)                                     | 10,525                                  | 80,992               | 12.99   |
| 1979-80 | 1,392 (11.6)                                      | 2,818 (23.5)                                   | 9,156 (76.5)                                     | 11,947                                  | 87,253               | 13.72   |
| 1980-81 | 1,311 (9.9)                                       | 2,998 (22.7)                                   | 10,182 (77.3)                                    | 13,180                                  | 1,04,201             | 12.65   |
| 1981-82 | 1,962 (12.5)                                      | 3,736 (24.0)                                   | 11,968 (76.0)                                    | 15,704                                  | 1,16,705 (E)         | 13.50   |
| (R.E.)  |   |  |  |   |                      |   |
| 1982-83 | 2,382 (12.9)                                      | 4,334 (23.6)                                   | 13,231 (76.4)                                    | 17,615                                  |                      |   |
| (B.E.)  |   |  |  |   |                      |   |
|         | -48*  | -54*   | +587*  | +533*                                   |                      |   |

\*Effect of Budget proposals, (E) = Estimated on the assumption of 4.5% growth in real terms (1970-71 prices) and 12% growth at (Current prices) over the previous year.

Source: Eastern Economist, Budget Number, 1982, V. 78, No. 11. March 19, 1982.

corporation tax in 1970-71, the share being raised to 43.7 per cent in 1980-81, 51.8 per cent in 1981-82 and 54.5 per cent in 1982-83. Therefore, it would be unwise to think for a while that the major contributory to the diminishing growth of direct taxes is corporation tax, rather it can be emphasised that the growth of corporation tax as a source of revenue collection by the Centre remains unabated almost for all the years under study. That increasing role of corporation tax is not only for the growth of corporate activity alone but also for the numerous discretionary changes experimented relating to corporate sector.

### 1.3. Tax Responsiveness:

For the purpose of finding out tax responsiveness, Table I.3 has been prepared.

The importance of tax as a source of revenue has been increasingly felt. The total tax revenue of the central and state governments as a percentage of national income increased from 7.4 per cent in 1951-52 to 18.7 per cent in 1978-79 and 19.7 per cent in 1979-80. But such tax-income ratio declined to 18 per cent in 1980-81. Paradoxically the national income at current prices rose by 19.4 per cent in the year 1980-81.<sup>2</sup> That might reflect the less responsiveness of our tax structure to the growth of national income and lack of built-

---

2. The Economic Times, Calcutta, Monday, Feb. 22, 1982.



Table - I.3

Combined Receipts of Central and State Governments:  
(1951-52 to 1980-81)

(Rs. ... Crores)

| Year    | Revenue Receipts | Tax Revenue | National income at current prices. | Tax Revenue as per cent of Revenue Receipts.<br>(Col. 3 as % of 2) | Tax Revenue as per cent of N.I.<br>(Col. 3 as % of 4) |
|---------|------------------|-------------|------------------------------------|--|---|
| 1       | 2                | 3           | 4                                  | 5  | 6   |
| 1951-52 | 906              | 741         | 9970                               | 81.8   | 7.4   |
| 1952-53 | 1051             | 768         | 9980                               | 73.1   | 7.7   |
| 1953-54 | 1161             | 891         | 11310                              | 76.7   | 7.9   |
| 1954-55 | 1710             | 1355        | 13263                              | 79.2   | 10.2  |
| 1955-56 | 1846             | 1537        | 13937                              | 83.3   | 11.0  |
| 1956-57 | 2484             | 1855        | 14795                              | 76.5   | 12.5  |
| 1957-58 | 2999             | 2313        | 16977                              | 77.1   | 13.6  |
| 1958-59 | 3330             | 2585        | 20001                              | 77.6   | 12.9  |
| 1959-60 | 3689             | 2902        | 20637                              | 78.7   | 14.1  |
| 1960-61 | 4026             | 3240        | 23848                              | 80.5   | 13.6  |
| 1961-62 | 4361             | 3423        | 28054                              | 78.5   | 12.2  |
| 1962-63 | 4846             | 3727        | 28607                              | 76.9   | 13.0  |
| 1963-64 | 5273             | 4182        | 31606                              | 79.3   | 13.2  |
| 1964-65 | 5810             | 4735        | 34368                              | 81.5   | 13.8  |
| 1965-66 | 6840             | 5565        | 36745                              | 81.4   | 15.1  |
| 1966-67 | 8233             | 6432        | 40422                              | 78.1   | 15.9  |
| 1967-68 | 9286             | 7363        | 50665                              | 79.3   | 14.5  |
| 1968-69 | 11616            | 9206        | 59315                              | 79.3   | 15.5  |
| 1969-70 | 14344            | 11155       | 61609                              | 77.8   | 13.1  |

Contd.....

Table - I.3 (Contd.....)

|         |       |       |         |      |      |
|---------|-------|-------|---------|------|------|
| 1976-77 | 15353 | 12294 | 66385 P | 77.5 | 18.4 |
| 1977-78 | 17257 | 13215 | 74794 P | 76.6 | 17.7 |
| 1978-79 | 19302 | 14967 | 80090 Q | 77.5 | 18.7 |
| (R.E.)  |       |       |         |      |      |
| 1979-80 |       |       |         |      | 19.7 |
| 1980-81 |       |       |         |      | 18.0 |

P = Provisional

Q = Quick Estimate

Source : Reserve Bank of India : Occasional Papers V. 2 No. 1 June, 1981.

in-flexibility.

That low responsiveness in case of corporate sector is not attributed to lower tax incidence but more due to low tax base. Unlike the personal income tax, the low base should not be identified as the result of tax evasion because of peculiar nature of corporate sector. It has been shown by Mr. V. G. Rao in his empirical study that the corporate enterprises' dependence on loan financing has gone up substantially and this has led to more than proportionate decrease in profits which form the base for "corporate taxation"<sup>3</sup>. He shown average percentage shares of the Four Factor Incomes in Net Value Added of Private Corporate Enterprises as

| Period             | Wages | Rent | Interest | Profits. |
|--------------------|-------|------|----------|----------|
| 1960-61 to 1964-65 | 55.38 | 2.10 | 3.96     | 38.56    |
| 1965-66 to 1969-70 | 59.74 | 2.43 | 6.76     | 31.07    |
| 1970-71 to 1974-75 | 61.52 | 2.06 | 10.06    | 26.36    |

Therefore it might be required to assess the need for changing the tax base.

Again in India tax is mainly mobilised from non-farm sectors though the agricultural sector itself contributes about 40 to 50 per cent of the national income. A large number of assesseees having higher income brackets arising from agricultural sources are now exempted from tax purview because of its non-taxable nature.

<sup>3</sup> V. G. Rao  
3. Business Standard, Calcutta. Annual 1982, pp. 77 to 81.

This has led to the development of a lopsided tax structure also.

#### 1.4: Effective incidence of tax\* on Corporate Sector:

Depending on the nature of activities and extent of income of companies the nominal rates of income - tax, additional income tax and companies (profits) sur tax together in India is more than 80% in average which no doubt, is high in comparison with the prevailing rates in other countries of the world. But the average effective rate might show another type of picture. Of course the effective rate of tax might vary from industry to industry but it could be said that bigger companies had progressively paid a lower rate of tax than the smaller companies. Avail-ling of different forms of rebates, reliefs and tax exemptions, the bigger companies might have managed the benefits of lower effective rates of taxes or even no taxes inspite of higher amount of profits. The various incentives and deductions allowed under different clauses of the Income tax Act had enabled 64 giant companies to be free from the tax burden inspite of the fact that they had made total profits of Rs. 252.87 crores during 1981-82.<sup>4</sup> So in the present circumstances the probable problem is not so much of high rates of income tax but how to distribute the different tax benefits amongst the small companies in order to avoid concentration of wealth.

---

4. The Economic Times, Calcutta, Thursday, March, 3, 1983  
(Research Bureau).

\* Provision for tax (PFT)/Profit before tax (PBT)

In a recent study made by corporate Investment Research & Consultancy Bureau, New Delhi, of 176 profit making companies covering 12 industries for a period of four years, 1977-78 to 1980-81, the results were -

(a) The average effective rate of tax for the corporate sector as a whole for the four years taken together was 44.2 per cent; (Table I.4).

(b) the average effective rates were 48 per cent in 1977-78, 43.7 per cent in 1978-79, 45 per cent in 1979-80 and 41.6 per cent in 1980-81; (Table I.4)

(c) the highest rate of tax on industries during the years were 81.2% for miscellaneous group in 1977-78, 93.2% and 82.3% for chemicals & pharmaceuticals in the years 1978-79 and 1980-81 respectively and 89% for sugar & plantation in 1979-80 but the average highest rate of tax in the four years period on chemicals and pharmaceuticals companies came to 93.2 per cent in 1978-79; (Table I.4)

(d) on classification of 176 companies according to total assets, the number of companies gradually diminishes, having total assets less than Rs. 50 crores but such figures increased in higher asset brackets; (Table I.5) and

(e) in tax - incidence wise classification of companies no clear cut trend had emerged though a slight trend might emerge

Table - I.4

## INCIDENCE OF TAX ACCORDING TO INDUSTRIES (YEARWISE RESULTS)

(1977-78 to 1980-81)

| Name of Industry          | FY | 1977-78          |           | 1978-79          |           | 1979-80          |           | 1980-81          |           | Average Effective Rate of tax for four years. |
|---------------------------|----|------------------|-----------|------------------|-----------|------------------|-----------|------------------|-----------|---|
|                           |    | Rate of tax in % |           | Rate of tax in % |           | Rate of tax in % |           | Rate of tax in % |           |   |
|                           |    | Highest          | Effective | Highest          | Effective | Highest          | Effective | Highest          | Effective |   |
| Textiles                  | 29 | 67.3             | 33.7      | 57.9             | 23.4      | 56.4             | 29.3      | 58.3             | 27.6      | 30.1  |
| Engineering               | 27 | 64.8             | 42.1      | 77.9             | 42.0      | 65.4             | 43.4      | 63.7             | 44.3      | 43.2  |
| Chemical & Pharmaceutical | 32 | 75.8             | 66.2      | 93.2             | 62.4      | 76.0             | 52.0      | 82.3             | 47.0      | 51.4  |
| Auto & Accessories        | 8  | 64.0             | 41.4      | 60.9             | 38.6      | 59.6             | 34.6      | 55.6             | 27.1      | 34.2  |
| Steel, Metal & Alloys.    | 10 | 58.7             | 37.9      | 69.7             | 33.6      | 66.6             | 42.5      | 72.2             | 47.6      | 41.5  |
| Cables & Electricals      | 16 | 71.1             | 59.7      | 69.0             | 57.9      | 68.8             | 58.9      | 67.7             | 58.4      | 53.7  |
| Paper                     | 3  | 57.3             | 43.7      | 54.3             | 40.4      | 53.5             | 42.4      | 35.9             | 33.4      | 39.5  |

Cont.....

Table - 1.4 (Contd.....)

| Shipping           | 1   | Nil  | Nil  | Nil  | 62.7 | 62.7 | 65.2 | 65.2 | 57.0 |
|--------------------|-----|------|------|------|------|------|------|------|------|
| Sugar & Plantation | 11  | 81.1 | 61.8 | 75.9 | 49.8 | 89.0 | 51.5 | 74.0 | 53.1 |
| Cement             | 8   | 67.1 | 55.4 | 72.5 | 49.8 | 73.4 | 52.1 | 43.7 | 51.8 |
| Electricity        | 6   | 67.3 | 56.5 | 68.9 | 53.9 | 68.1 | 46.6 | 46.3 | 44.2 |
| Miscellaneous      | 25  | 81.2 | 40.6 | 76.0 | 46.5 | 76.5 | 50.5 | 75.4 | 47.1 |
|                    | 176 | 81.2 | 48.0 | 93.2 | 43.7 | 89.0 | 45.0 | 82.3 | 44.2 |

Source : Corporate Investment & Consultancy Bureau, New Delhi V. 1 No. 37, 19th July, 1982.

NORTH BENGAL  
UNIVERSITY LIBRARY  
RAJA RAMMOHUNPUR

1005926  
JUN 1984

Table - I.5

VARIATION IN INCIDENCE OF TAX ON COMPANIES : 1977-78 to 1980-81

(ASSETS WISE RESULTS)

| Size (Total assets)<br>Rs. in Crores | No. of |         | No. of |         | No. of |         |
|--------------------------------------|--------|---------|--------|---------|--------|---------|
|                                      | Cos.   | E.R.(%) | Cos.   | E.R.(%) | Cos.   | E.R.(%) |
|                                      | 1977   | - 1978  | 1978   | - 1979  | 1979   | - 1980  |
| Below 50                             | 141    | 48.9    | 134    | 45.4    | 124    | 49.0    |
| 50 - 100                             | 26     | 48.5    | 30     | 41.6    | 33     | 43.2    |
| 100 - 150                            | 6      | 55.3    | 9      | 51.7    | 13     | 43.9    |
| 150 - 200                            | 1      | 40.3    | 1      | 41.6    | 4      | 45.6    |
| 200 and above                        | 2      | 20.6    | 2      | 13.4    | 2      | 21.2    |
|                                      | 176    | 48.0    | 176    | 43.7    | 176    | 45.0    |
|                                      |        |         |        |         | 176    | 41.6    |

Source : Corporate Investment & Consultancy Bureau, New Delhi, V.1 No. 37, 19th July, 1982.



that bigger companies were paying lower rate of tax (Table I.5)

So, it might be evident from the study that there are ample scopes of rationalisation of the tax structure by giving benefits to the smaller companies.

#### 1.5. Objectives of the Study:

In India the goal of development is "socialistic" but India being a "mixed" economy private corporate sector plays a big role in creation of employment, savings and income. Private enterprises in general and corporate sector in particular can function smoothly and contribute to development only in an appropriate public policy environment. But it remains an overriding challenge to government in all developing countries to create a congenial environment of public policies that will encourage and enforce competitiveness and efficiency. Limitations on the role of the private sector are usually established in practice either by economic factors or by national political considerations. In both the cases corporate tax is a very important tool to understand the behaviour of the private sector.

The diverse experiences of the developing countries clearly demonstrate that there is no single road to development. Large countries well endowed with natural resources, have more options than those that are small and poorly endowed, but all must choose a combination of development policies that will help them

fulfil their own particular aspirations. The evidence suggests that those countries that have grown most rapidly have adopted a policy framework that enables private enterprises to thrive. The creation of an economic climate that is conducive to development requires a clearly defined tax policy.

In advanced countries as a considerable proportion of economic activity is organised in the form of corporate bodies, company profits constitute a major source of revenue. The importance of this sector in the developing countries like India is growing.

The modern form of company taxation is a tax on the undistributed profits of companies and it embodies the principle of ability to pay. It has now developed into an impersonal system of taxation. Two kinds of ideas have influenced the development of corporate taxation. The first is that a company is nothing but an aggregate of a number of shareholders banded together for the achievement of some common purpose under limited liability; it is difficult to impose the personal income tax upon all the shareholders and needless to impose the tax upon corporate income. The second approach is that since the general law of the land entitles a corporation with a personality of its own and regards it as an entity distinct from the shareholders, a corporation owes a duty to pay tax on its income apart from the income tax on the shareholders' income. The two-tier system of corporate

taxation in Burma, Japan, India and Pakistan until 1960 is based on these two ideas. It has been alleged that the rate of taxation in most of the developing countries is higher than the developed countries. In India, the rate of corporate taxation is definitely higher than most of the advanced countries but the effect is moderated by different rebates combined with depreciation allowances and tax-holiday benefits to producing industries.

It is true that the manipulation of the tax mechanism is not likely to produce the desired result for development alone and no single panacea can be prescribed to cross the barriers of investment, savings, employment and capital formation; but corporate sector is accepted to play a big role for the economic development of any country and proper tax policy is essential to study the quality of corporate tax structure in India and its impact on the activities of the corporate sector.

The purpose of this dissertation is to study the evolution, nature and problems connected with the corporate tax structure in India. More specifically it can be said that our study will high-light the evolution of corporate tax system in India and analyse the present form of corporate tax structure and indicate its effect on corporate behaviour.

How corporate bodies react to the imposition of taxation might be taken for our purpose as corporate behaviour. The direct and even indirect effect of corporate taxation on corporate

bodies are analysed in our study both at macro and micro level. Specifically the impact of taxation on corporate investment, corporate tax savings, employability, financial structure, profitability and probable tendency of shifting the incidence, either forward or backward, are some of the areas which are covered in this study. It would be our attempt to find out the relationship, if any, of such behaviour of corporate bodies with the corporate taxation.

#### 1.6. Plan of the work:

The whole work has been divided into seven chapters. The second chapter has been devoted to the evolution of corporate taxation since the inception of taxation legislation in India. The chapter is meant for finding out the notable landmarks in the taxation history over the last century and the reasons for such change. The third chapter will analyse the existing corporate - tax structure in general and the classification of companies for the purpose of taxation, basic rates of taxation depending on range of income and nature of companies, additional income tax, sur tax and different exemptions, reliefs, rebates in particular. The same chapter will also give some suggestions as to how the present tax structure should be rationalised and simplified. In the fourth chapter we have tried to show the implications of corporate taxation on corporate behaviour from

different angles like impact of tax on corporate investment in fixed assets, tax savings, its employment pattern, size, profitability, incidence and shifting, concentration of wealth and on various other related matters <sup>at</sup> ~~in~~ the macro level. Fifth and sixth chapters are specifically designed to show the impact of tax on their behaviour pattern in the form of case studies of two companies, one from public Sector and the other from Private Sector, in chemical industry. The seventh, the last chapter, will show the summary of all the chapters and will highlight the recommendations and concluding observations regarding the existing system of corporate taxation in India.

#### 1.7. Methodology and Limitations of data:

To study the nature, quality and behaviour of corporate tax in India, vis-a-vis its impact on corporate bodies, we have used a methodology which may be termed as "U.N. Technique" to study a particular problem. In this context two other techniques need little discussion.

One can approach a particular problem by using mathematical models and econometric analysis. One difficulty with this methodology is that the data must be of good quality and time series data are available for a long period. Further, Mrs. Helen Makower has shown that econometric analysis is difficult to build up and easy to demolish. Quality of data, in our analysis

is such that it is not really amenable to mathematical model building and its testing.

In the other extreme, we could have a descriptive type of analysis without referring to data or to theoretical analysis. This type of analysis was very popular in the mid-fifties.

But we have adopted a technique which is neither descriptive nor mathematical. In other words, we have avoided strict econometric technique but have gone through the regours of case studies, historical development, macro analysis as well as micro studies. This is known as "U. N. technique" of analysis, because most of the books published under the auspices of the U.N.O. more or less undertake an approach which is neither mathematical nor an exercise of model building. In this technique theories are brought in to understand the data whenever it is required and past data are analysed to throw light on the current issues and from the analysis of data, certain conclusions are drawn after testing the hypothesis made in the appropriate areas.

It is needless to say that in underdeveloped countries like India, data are not easily available even for the organised sectors. Even if data are available, these are not strictly comparable. Even if it is comparable, sources are highly suspect or data may be manipulative<sup>ed</sup> to bring home certain a priori conclusion. Therefore, we have to be very cautious in choosing data and

come to some conclusion from the same. So under the limitation of the quality of data, we have depended upon government sources and audited accounts of the companies concerned to a great extent. Again the data are not available systematically and continuously.

Within this limitation we have conducted our research and have come to certain tentative conclusions.

We took the help of different reports of the Government of India, specially of Kaldor Committee's Report, Choksi Committee's Report and Dandekar Committee's Report for the purpose of showing the evolution of corporate taxation and to give an insight as to how to simplify and rationalise the existing corporate tax structure. The annual budgets of the Government of India and the publications, like All India Income tax statistics, Reserve Bank of India Bulletins, I.C.I.C.I.'s Portfolio Analysis, Tata Research Centre's financial analysis, Stock Exchange Directory and reputed journals on Commerce and economics like Chartered Accountant, Management Accountant, Eastern Economist, Economic and Political weekly, Income tax Digest, Commerce, Capital, Joint Stock Companies - news and notes, Circon Review etc. are also used in different chapters. Economic/ Times, Business standard and some other established daily news papers are also being used. The contemporary published and unpublished different thesis based on corporate taxation, and authentic books on taxations, national and international, have also been referred to. The source like I.M.F.

review has also been utilised for showing the comparative tax structure from the international perspective.

For the fourth chapter we have utilised the aggregate accounting and other figures of number of companies in different industries from the Balance sheets, Revenue Accounts and statements, showing the sources and utilisation of funds and the like from different sources, specially from R.B.I. Bulletins, I.C.I.C.I.-Portfolio Analysis 1981, Tata Research Centres - financial analysis and corporate Investment Research and Consultancy Bureau's review. A number of Tables have been prepared for the purpose of analysis vis-a-vis the impact of corporate taxation on corporate behaviour.

Fifth and sixth chapters are mainly based on the Companies' Annual Reports covering the financial period from 1976-77 to 1980-81. A number of Tables have also been prepared from such Annual Accounts which are duly analysed to find out the probable relationship between the tax imposed on such companies and their behavioural pattern in different aspects. Annual Review of chemical industries sponsored by 'Commerce' in different years are also analysed as background material in the fifth Chapter.

In other words, our study will be an empirical one by taking data from different sources. The data will be arranged and processed to throw light on the corporate tax and its impact



on the industries in particular and on the economy in general.

### 1.8. An overview of the literature and research gap:

There are various books and articles on Corporate Tax in India. Inspite of the existence of this literature there is a huge research gap.

Prof. V. G. Rao in his empirical study has attempted to show that because of increasing impact of loan financing of the corporate bodies there had been a visible proportionate decrease of taxable profits. He has further shown that the corporate tax revenue has not increased pari passu with the growth of national income.

The books written by eminent tax experts in India like N.A. Palkhivala, S. Bhattacharya are nothing but relating to law and practice of taxation.

There are number of books published and unpublished on the evolution of corporate tax in India. In this context, Prof. J. P. Niyogi's book published in 1939 has become out of date. The unpublished thesis of Dr. A. K. Roy is mainly historical rather than analytical. The same is true in the work of S. Ambirajan. The book of Mistry & Kumar is mainly concerned with tax planning aspect. Mohammad Mohsin in his book shown only the scope of rationalisation of corporate tax structure.

Many other books written by different authors like P. N. Banerjee, A. K. Jain, R. N. Lakhotia, S. K. Mukherjee, G. L. Pophale, G. S. Sahota are definitely of great importance but none of these books deal with corporate behaviour and its relationship with corporate tax structure.

The unpublished thesis of Dr. B. Chakraborty is mainly econometric. He has tried to test the hypothesis whether the incidence of corporate tax can be shifted forward or backward. Partha Sarathi Shome also tried to measure the magnitude and direction of shifting of the tax burden. This type of analysis is no doubt important but leaves a scope for understanding the impact of corporate tax on corporate behaviour especially in respect to savings potential and employment generation in a country like India.

Apart from these books there are number of articles based on fact findings by many research bureaus in different recognised journals and newspapers. But it can be said that most of the articles are not suggestive but descriptive in nature.

It is true that there are innumerable number of government reports and reports of commissions and of study groups concerning taxation in India. Like most of the reports, analysis in such reports is very often "narrative" namely, the reports deal mainly with policy prescription without having much of a "positive" basis, i.e. to say, what are the problems associated with corporate tax at a point of time and over a period of time. Further, the

reports mainly deal with rationalisation of tax structure, which is often influenced by the prevailing value judgement of a particular Government in power. Hence, almost all the reports are very quick in generalisation without having much of the data base or analytical superstructure.

It is in this context, we humbly consider that there is a definite research gap in the analysis of corporate tax. None of the books or reports mentioned above deal with the problem of impact of corporate tax on (say) liquidity position of the companies, though some of the contemporary authors have analysed the liquidity and working capital problem in the corporate bodies but they have also failed to show the tax aspect in that regard. Further, in most of the books problems regarding employment, savings, capital formation and investment has been given a scant attention. None of the reports or books have ever referred to any micro-problem or dealt with selective case studies.

Therefore, this dissertation is a modest attempt to fill up the research gap in this field. It is needless to mention that data are difficult to collect and collate. Under the limitations of data in the context of an underdeveloped economy like India we have made an attempt to look into the problems of corporate taxation in India and certain specific behaviours of corporate bodies hitherto neglected.